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TRADE AND DEVELOPMENT BOARD
Nineteenth special session
Bangkok, 29 April – 2 May 2002
Item 1 (a) of the provisional agenda

PROVISIONAL AGENDA AND ANNOTATIONS

I. Provisional agenda

1. Procedural matters:
   - (a) Adoption of the agenda and organization of the work of the session
   - (b) Report on credentials
2. Mid-term Review
   - (a) Review of the efficiency and functioning of the intergovernmental machinery
   - (b) Stocktaking in respect of the implementation of the commitments and work programme agreed to in the Bangkok Plan of Action
   - (c) Interactive debates and policy dialogue in the context of opportunities and challenges of new policy developments of importance since UNCTAD X:
     - (i) Assessment of global economic developments and their impact since UNCTAD X
     - (ii) Development challenges of the future
3. Institutional, organizational, administrative and related matters:
   - Administrative and financial implications of the actions of the Board
4. Other business
5. Adoption of the report of the Board

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II. ANNOTATIONS

1. At its twenty-fourth executive session in May 2000, the Trade and Development Board adopted the following decision: "The Trade and Development Board will conduct in the second quarter of the year 2002 a mid-term review of the work of UNCTAD, based on the indicators of achievement agreed to in the medium-term plan (2002-2005). The Board will also review the functioning of the intergovernmental machinery."

2. At its forty-eighth session, in October 2001, the Board agreed to endorse the offer of Thailand to host the Mid-term Review in Bangkok, launched the mid-term review process and approved the basic modalities of the Mid-term Review process, as outlined in document TD/B/48/CRP.1, namely: (i) a review of the efficiency and functioning of the intergovernmental machinery; (ii) stocktaking in respect of the implementation of the commitments and work programme agreed to in the Bangkok Plan of Action (TD/386); and (iii) interactive debates and policy dialogue in the context of opportunities and challenges of new policy developments of importance since UNCTAD X.

3. In its resolution 56/178 of 21 December 2001, the General Assembly welcomed the decision by the Trade and Development Board to conduct the mid-term review of the outcome of the tenth session of the United Nations Conference on Trade and Development at Bangkok from 29 April to 3 May 2002, and, in this regard, expressed deep appreciation to the Government of Thailand for offering to host the meeting.

Item 1. Procedural matters

(a) Adoption of the agenda and organization of the work of the session

4. The provisional agenda for the current session is reproduced in section I above.

	Documentation
TD/B/(S-XIX)/1	Provisional agenda and annotations

Organization of work

5. In order to accommodate suggestions made by delegations, meetings of the session of the Board have been organized in such a way that no two meetings take place at the same time. They have been designed with a view to ensuring effective participation by delegations, particularly that of small delegations, and also to making the most efficient use of the conference resources of the United Nations. A programme of meetings is annexed to the present document.

(b) Report on credentials

6. In accordance with rule 17.2 of the rules of procedure, the Bureau of the Board shall examine the credentials and submit its report to the Board.

In-session documentation

Item 2. Mid-term Review

7. At its forty-eighth session, the Board agreed that three Vice-Presidents would assist the President in the preparatory work for the Mid-term Review, as follows: on the intergovernmental machinery – Mr. Federico Alberto Cuello Camilo (Dominican Republic); on the stocktaking of the implementation of the work programme based on indicators of achievement – Mrs. Eleanor M. Fuller (United Kingdom); on the interactive debates and policy dialogue in the context of opportunities and challenges of new policy developments of importance since UNCTAD X – Mr. Virasakdi Futrakul (Thailand). The two Vice-Presidents in charge of the intergovernmental machinery and stocktaking would make every effort to conclude their work prior to the Mid-term Review in Bangkok.

(a) Review of the efficiency and functioning of the intergovernmental machinery

8. At its twenty-fourth executive session, the Trade and Development Board decided to "Review the functioning of the intergovernmental machinery" in the context of the Mid-term Review. Under this sub-item, the Chairperson of Pillar I will present a report on the review of the intergovernmental machinery to the Trade and Development Board for its approval and adoption. The review undertaken has been aimed at improving the functioning of intergovernmental bodies of UNCTAD to better respond to requirements of UNCTAD's member States, in particular the needs of developing countries.

(b) Stocktaking in respect of the implementation of the commitments and work Programme agreed to in the Bangkok Plan of Action

9. At its twenty-fourth executive session, the Trade and Development Board decided to "conduct in the second quarter of the year 2002 a mid-term review of the work of UNCTAD, based on the indicators of achievement agreed to in the medium-term plan (2002-2005)". Accordingly, an in-depth assessment of the implementation of the Bangkok Plan of Action and achievements since UNCTAD X was conducted on a subprogramme-by-subprogramme basis during the meetings of the mid-term review from January to March. At the same time, the future direction of work and the areas of emphasis for the remaining period until the next Conference were discussed with a view to making progress in the implementation of the Plan in the most effective manner, taking account of the existing resource constraints, and reflecting the latest developments since UNCTAD X, such as the outcomes of the Third United Nations Conference on the Least Developed Countries (Brussels, May 2001), the Fourth Ministerial Conference of the World Trade Organization (Doha, November 2001) and the International Conference on Financing for Development (Monterrey, March 2001).

(c) Interactive debates and policy dialogue in the context of opportunities and challenges of new policy developments of importance since UNCTAD X

10. It is envisaged that two high-level sessions of interactive debate and policy dialogue will be held on Wednesday, 1 May, and Thursday, 2 May, in Bangkok in the context of the Mid-term Review at the nineteenth special session of the Trade and Development Board namely:

(i) Assessment of global economic developments and their impact since UNCTAD X;

(ii) Development challenges of the future.

11. The first of these sessions will assess global economic developments and their impact since UNCTAD X by addressing the topic of economic policy challenges since the adoption of the Bangkok Plan of Action in February 2000. The second session of the high-level debate will be orientated to future development challenges by addressing the topic of rethinking development strategies and reshaping globalization.

12. The policy debate on the above two themes, assessing the past and looking forward to the future, will be underpinned by the outcome of the other two pillars on the efficiency and functioning of the intergovernmental machinery of UNCTAD and the stocktaking in respect of the implementation of the Bangkok Plan of Action. The specific objective is to bring forth ideas and policy directions on the challenges for members of UNCTAD after the Mid-term Review and consequently serve as a prelude to identifying potential elements of relevance for UNCTAD XI.

Item 3 - Institutional, organizational, administrative and related matters:

- **Administrative and financial implications of the actions of the Board**

13. The Board will be informed during the session of the administrative and financial implications of any proposals before it.

In-session documentation, if required

Item 4 - Other business

Item 5 -. Adoption of the report of the Board

14. The Board may wish to authorize the Rapporteur to finalize the report on its nineteenth special session under the authority of the President.

PROGRAMME OF MEETINGS
Nineteenth special session of the Trade and Development Board - Mid-term Review
29 April – 2 May 2002

Monday 29 April 2002	Tuesday 30 April 2002	Wednesday 1 May 2002	Thursday 2 May 2002	Friday 3 May 2002
REGISTRATION UNCC-ESCAP Registration Counter **(09h30 to 12h00** **14h00 to 18h00)**	**PLENARY** ESCAP HALL **(10h00)** Opening plenary Item 1 – Procedural matters Item 1(a) Adoption of the agenda Item 2 – Mid-term review (Reports of the three Vice-Presidents on items 2(a), (b) and (c))	**FIRST HIGH-LEVEL INTERACTIVE DEBATE** ESCAP HALL **(09h00)** Item 2 (c) (i)- Assessment of global economic developments and their impact	**SECOND HIGH-LEVEL INTERACTIVE DEBATE** ESCAP HALL **(09h00)** Item 2 (c) (ii) - Development challenges of the future	***HOST COUNTRY EVENT***
BRIEFING FOR PARTICIPANTS Public Foyer **(16h00)**	**INAUGURAL CEREMONY** ESCAP HALL **15h20** Participants to be seated **15h30** Inaugural ceremony	*INAUGURATION OF THE INTERNATIONAL INSTITUTE FOR TRADE AND DEVELOPMENT* (Chulalongkorn University) Buses will leave ESCAP premises at **14h30**	*INAUGURATION OF ACIS RAILTRACKER* **15h30** **PLENARY** ESCAP HALL **(17h00)** Closing plenary Item 1(b) – Report on credentials Item 2 – Mid-term review Item 3 – Admin & financ. implicat. Item 4 – Other business Item 5 – Adoption of the report **Followed by** Press Conference	

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TRADE AND DEVELOPMENT BOARD
Nineteen special session
Bangkok, 29 April 2002
Item 2(c) of the provisional agenda

MID-TERM REVIEW

Interactive debates and policy dialogue in the context of opportunities and challenges of new policy developments of importance since UNCTAD X

Issues note by the UNCTAD secretariat

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MID-TERM REVIEW: INTERACTIVE DEBATES
ISSUES AT STAKE

A. The global economy since UNCTAD X

1. UNCTAD X took place at a time of reviving optimism in the global economy. Many crisis-stricken East Asian economies were enjoying growth rates close to those reached in the first half of the 1990s, exchange rates were stabilizing, interest rate spreads in international markets had narrowed significantly, and foreign capital had begun to return. In Latin America, recovery from the aftershocks of the Asian financial crisis had been slower, but growth rates were climbing above the average for the previous decade and FDI was flowing back into the region. Although sub-Saharan Africa was still not showing the same vibrancy, some of the region's biggest economies looked poised for more sustained growth. Prospects were buoyed by the expectation that continued strong growth in the United States would fuel export demand elsewhere, and by a belief that Europe was beginning to move on to a path of faster growth, adding a second locomotive to the world economy.

2. That optimism has proved short-lived. The world economy slowed sharply in 2001, pulled down by weak performances in all three leading economic regions in the developed world. The high-technology boom in the United States burst soon after UNCTAD X ended, slowing the economy, which eventually tipped into recession in the course of last year. The belief that the euro area would be immune to slowdown in the United States proved unfounded. Faltering exports, drops in profits of affiliates in the United States, and an overly cautious monetary and fiscal response all contributed to a sharp decline in the growth rate last year, which has stabilized unemployment at a relatively high level. The global slowdown also upset the tentative recovery that had begun in Japan in 2000, sending the economy back into recession.

3. Developing countries have very quickly felt the impact of the slowdown in the major industrial countries, with their overall growth dropping to about 2 per cent in 2001 from about 5.5 per cent in the previous year. East Asia has led the downswing, with several countries experiencing a return to recession conditions in 2001. Latin America has followed, with a marked slowdown in some of the largest economies, notably Brazil and Mexico. Growth in Africa has remained at a level that barely matches the rate of population growth. Only China and India, two big economies which depend less on foreign trade, have escaped the downward pressure from world markets.

4. In today's increasingly interdependent world, developing countries are more vulnerable than in the past to disturbances emanating from the advanced industrial core. International trade has been an important channel in transmitting the slowdown in the industrial countries. After growing by 14 per cent in 2000, export volumes for developing countries grew less than 1 per cent in 2001, with all major regions experiencing a sharp slowdown. Many developing countries in East Asia have seen sharp drops in their export earnings from products such as electronics where they have expanded capacity in recent

years. In many regions, slower growth in export volumes has been compounded by lower prices, particularly those of primary commodities.

5. Finance has been another channel of transmission. Uncertainty surrounding emerging market prospects has left private international capital flows to developing countries well below the pre-1997 levels, and only FDI has remained buoyant, albeit heavily skewed towards a small number of locations. The expectation that economic slowdown and looser monetary policy in the industrial countries would trigger capital flows to developing countries, as was the case in the early 1990s, has not happened. Rather, increased risk aversion and liquidity preference have led a flight to safety and added to the strength of the dollar, which has reached, in real effective terms, the levels observed in the mid-1980s before the Plaza agreement on intervention to bring an orderly devaluation. While domestic economic difficulties no doubt played a key role in the outbreak of a new round of financial crises in Argentina and Turkey, external factors also contributed: not only the slowdown in industrial countries but also the strength of the dollar weakened trade performance in these countries since they were both pegging their currencies to the dollar (a fixed peg in Argentina and a crawling peg in Turkey).

6. Despite the concerted response from the world's most important central banks following the events of 11 September, only in the United States has policy been consistently focussed on attaining a rapid recovery by reviving domestic spending. By contrast, economic performance in the euro area and Japan continued to depend on expansion of foreign demand. Many of the East Asian developing countries with relatively favourable external payments positions have sought to mobilize domestic sources of growth through expansionary macroeconomic policies and attained some recovery in the latter part of 2001. However, most developing countries, notably in Latin America and Africa, have had little room to expand domestic demand owing to tighter external constraint due to falling export earnings and private capital inflows.

7. There were widespread expectations that a positive outcome in Doha would help accelerate economic recovery and expansion of trade by raising business and household confidence. The agreement reached did cover a comprehensive programme of work, defined partly as a response to the need to rebalance the rules of the trading system so as to alleviate the problems encountered by developing countries as well as to the need to bring greater consistency between the macroeconomic and development dimensions of trade. However, the impact on major macroeconomic trends of an agreement on an agenda per se is limited largely to avoidance of the shock to confidence which might have resulted from failure at Doha. Further favourable effects depend on the eventual outcome of the negotiations. Moreover, the agreement in Doha has not prevented the emergence of new frictions in the trading system as the combination of economic slowdown, the strength of the dollar, and large and persistent trade imbalances have provided humus to renewed protectionist pressures.

8. Global prospects hinge crucially on policy actions designed to restore strong recovery in private spending in the leading industrial economies. The United States has taken the boldest measures with a series of expansionary fiscal and monetary actions, which were

accelerated after 11 September. Still the legacy of indebtedness created during the boom years may prove difficult to shake off, and there is uncertainty surrounding the likely strength of the country's recovery. In Europe, the Stability and Growth Pact has led to the pursuit of budget deficit targets with insufficient regard to countries' cyclical positions, and monetary policy has remained focussed primarily on inflation despite a sharp slowdown in economic activity. While a weak euro has helped to sustain foreign demand, from a global perspective monetary policy in the euro area has been restrictive in terms of the contribution of the region to global demand expansion. Absent a strong domestic demand-led recovery, it seems unlikely that Europe will take the lead from the United States in pulling the world economy back to faster growth. There are few signs of a quick turnaround for Japan, where exports are also expected to provide the stimulus and policy options are heavily circumscribed by structural weaknesses.

9. An orderly transition to a world where all the leading economies are pulling forcefully in the same direction is further complicated by the uncertainty surrounding exchange rate misalignments and by large and persistent trade imbalances. The strength of the dollar has been adding to global imbalances resulting from disparities in demand creation among the major industrial countries. If an increasing number of countries seek to depreciate their currencies against the dollar as part of their attempts to get out of the recession, the eventual correction needed for the dollar could become very large, creating a risk of sharp swings in major exchange rates with attendant consequences for financial stability and economic growth in developing countries. Avoiding such a risk requires a better balance in the contribution of major industrial countries to global demand, with Europe in particular taking greater responsibility.

10. Past experience suggests that growth in the industrial world needs to reach about 3 per cent in order to support a vigorous increase in employment and income in developing countries. On current trends and policies this is unlikely to happen in the near future. It is thus unlikely that there will be substantial increases in demand for developing country exports, a major recovery in commodity prices, or a strong increase in capital inflows to offset tighter external constraints. The context of slow and volatile growth, currency misalignments, and trade imbalances may also undermine efforts to improve market access for the exports of developing countries and holds out the threat of renewed protectionist pressures.

11. It may thus be necessary to reorient macroeconomic and structural policies in the industrial world outside the United States so as to bring faster and more balanced growth in the world economy. This is also necessary for averting the threat of protectionism and disruption of the efforts that began in Doha. Improved market opportunities could provide a useful boost to activity in developing countries, and increased use of regional trade and financing mechanisms may provide relief from external constraints and protection against financial instability. Still, a large number of developing countries will continue to require substantial official financial support if they are to be protected from the effects of the difficult external economic environment.

B. Reshaping globalization: in search of greater coherence

12. The developments in the world economy since UNCTAD X and the current uncertainties surrounding economic prospects have confirmed that most developing countries suffer from structural weaknesses that increase their vulnerability to external shocks and reduce their ability to sustain rapid growth. These weaknesses arise in part from the modalities of their participation in international trading and financial systems. Tackling such problems through appropriate development strategies will be taken up in the following section. But recent events also show that current global arrangements cannot always be relied upon to ensure financial and monetary stability and to sustain an expansion of employment, output and trade capable of lifting all boats together:

- Initiatives taken in the context of the reform of the international financial architecture since the outbreak of the East Asian financial crisis have not been very effective in preventing a new round of financial crises in emerging markets. In particular the Argentinian crisis shows the fragility of recourse to simple rules in the search for lasting stability. Again measures so far adopted for a better management of financial crises appear to be largely ineffective in preventing deep recessions and sharp increases in poverty in countries facing rapid exit of capital. Lack of effective international arrangements for orderly debt work-out procedures continues to create difficulties and uncertainties in the resolution of debt crises in emerging markets. All these point to the need to reconsider and reassess the reform process under way.

- The tightened external payments constraint on developing countries resulting from the recent downturn in the world economy and from the pro-cyclical behaviour of financial markets raises the question of the adequacy of multilateral arrangements for the provision of official balance of payments financing.

- The question of stability and appropriate alignment of exchange rates among the G-3 currencies remains unresolved, so that large swings continue to pose threats to global financial stability and the international trading system.

- Notwithstanding the concerted monetary policy response to 11 September, there has been little coordination of macroeconomic policies among the major industrial countries to provide the basis for a rapid and balanced expansion of global demand and to avert the build-up of further trade imbalances and protectionist pressures.

- While the Doha meeting acknowledged many of the concerns of developing countries first expressed in Seattle, there are considerable uncertainties surrounding the efforts at translating an expanded negotiation agenda into a genuine development agenda.

13. What is at stake is how to ensure that current arrangements in the different economic spheres of trade, finance, debt, investment, and technology mutually reinforce each other in support of equitable, rapid and sustainable growth and development. In a world of increased interdependence no country can put its house in order regardless of the conditions prevailing in its external economic environment. This is true not only for developing countries with their

well known weaknesses in absorbing external shocks, but also for the most powerful industrial economies.

14. The question of policy coherence and coordination on financial, trade and development issues was a priority for the architects of the post-war international economic order in the two international conferences in Bretton Woods and Havana. The discussions at these conferences were motivated by the objective of achieving lasting improvements in economic welfare through the pursuit of policies designed to attain full employment and rapid growth in the context of international monetary and financial stability. It was believed that attaining these goals would provide the basis for a rapid expansion of international trade and greater economic integration. Thus, the IMF was meant to ensure that countries facing balance-of-payments problems would not be forced to undertake destabilizing and deflationary adjustments by recourse to currency devaluations or retrenchment in domestic spending, which would threaten to disrupt growth, stability and international trade. The effectiveness of the arrangements agreed to at Bretton Woods thus required control over destabilizing capital flows to secure currency stability and the provision of sufficient international liquidity to prevent deflationary adjustments. It also depended on the provision of longer-term official flows through a second institution, the IBRD, to help build domestic productive capacity. A third institution, the ITO, was envisaged to ensure policy coherence and coordination on economic, financial, trade and development issues. In the event, the ITO failed to come into existence, and the resulting gap was only partly filled by GATT.

15. Despite various shortcomings in these arrangements, the world economy attained very strong growth combined with full employment in industrial countries until the late 1960s. During this period developing countries adopted a range of development strategies from import-substitution industrialization, popular in much of Latin America and Africa, to the more outward-oriented models adopted by some East Asian countries. Both models registered successes and failures, but growth in developing countries was on average fast by historical standards and often accompanied by profound economic, political and social changes. Multilateral lending and official development assistance along with trade preferences helped offset some of the long-standing asymmetries and biases in the international economy that have historically hindered growth in poorer countries.

16. Given the shortcomings of the post-war international economic architecture that became increasingly apparent in the late 1960s and eventually led to its demise in the early 1970s, there was clearly a need for reform of multilateral arrangements and global policies in order to ensure greater flexibility in responding to changes in the world economy. But the pendulum appears to have swung too far from conscious design and in much too disorderly a way. The international financial and trading system that has evolved since the breakdown of Bretton Woods has favoured private capital flows over official flows, exchange rate flexibility over stability, austerity over reflation, adjustment over financing, and creditors over debtors. It has moved international trade towards a single-tier system of rights and obligations, in which developing countries have generally the same level of obligations as the developed countries. Commitment to full employment has weakened, replaced by a focus on price stability. Trade liberalization and expansion have been put in front of economic growth and full employment, thereby rekindling mercantilist agendas.

17. Recent experience has raised questions, particularly from developing countries, about the effectiveness of current arrangements and the need for reforms to bring back a greater degree of coherence. A source of these concerns is that there are destabilizing and deflationary feedbacks among various spheres of economic activity, particularly trade, debt and finance, which often create impediments to development:

- Rather than being governed by comparative advantages, trade flows are frequently distorted by unstable and misaligned exchange rates with little relation to underlying economic fundamentals. This weakens the theoretical arguments advanced in favour of trade liberalization. Indeed, it can be argued, perversely, that in a world where exchange rates distort trade flows and global resource allocation, tariffs and subsidies may assume corrective roles. This problem is ignored in current global arrangements, which are based on a false dichotomy between trade and finance.

- By altering the relative competitive positions of various industries across countries, currency movements unrelated to economic fundamentals have the potential to trigger trade frictions and protectionism, undermining the international trading system. Exchange-rate misalignments have played an important part in recent trade disputes over shipping and steel.

- Shifts in international capital flows can also generate sharp swings in international trade flows by creating boom-bust cycles in economic activity. As seen during the East Asian crises and the more recent information-communication technology cycle in the United States, financial booms can lead to excessive expansion of investment, production and trade in particular sectors, which eventually comes to an end with the bursting of the bubble, resulting in sharp swings in trade flows and prices.

- Destabilizing linkages between trade and finance also operate through the cost and availability of external financing. Since assessments of creditworthiness determine access to trade financing from both the public and private sectors, financial crises can make not only importing but also exporting more difficult even after large devaluations and improvements in competitiveness. In the same vein, trade shocks lead to increased debt burdens and reduced capital inflows as they feed into higher risk spreads.

- While the post-war arrangements were founded on the belief that adverse influences emanating from trade, finance and debt should not be countered through measures sacrificing growth and development, under the present arrangements and policy approach, developing countries almost invariably find themselves obliged to absorb such influences through domestic retrenchment. As witnessed during the debt crisis of the 1980s as well as the more recent episodes of financial crises in emerging markets, adjustments to a tightening of the external financial constraint resulting from declines in export prices and earnings, increases in the external debt burden or cut-backs in international lending and investment typically take place through reductions in imports and economic activity, thereby exerting contractionary effects on world trade. Moreover, current rules of the trading system do not allow much room to countries to undertake import cuts on a selective basis so as to minimize their adverse effects on capacity utilization, capital accumulation and poverty.

18. Quite apart from such destabilizing and deflationary feedbacks among various spheres of economic activity, there are also concerns that global arrangements in trade, finance, debt, investment and technology contain systemic biases and asymmetries that constrain development:

- Despite the general acceptance of the benefits of free trade, the international division of labour is greatly influenced by commercial policies which favour products and markets in which more advanced countries have a competitive edge. High tariffs, tariff escalation, and subsidies in agriculture and fisheries are applied to products that offer a potential for export diversification in the developing countries. The panorama of protectionism is no better for industrial products including footwear, clothing and textiles where many developing countries have competitive advantages. The abuse of anti-dumping procedures and product standards against successful developing-country exporters creates further obstacles.

- There is an inconsistency between the policy advice given by multilateral institutions to developing countries in favour of import liberalization and export-oriented growth strategies – advice which is often reflected in conditionalities attached to their lending in the context of structural adjustment programmes – and the continued protectionism in some industrial countries' markets for dynamic agricultural and labour-intensive products. Furthermore, through the promotion of unilateral trade liberalization beyond WTO commitments, developing countries are deprived of the means to gain concessions on market access in subsequent trade negotiations.

- For most developing countries, the current working of the international trade and finance systems do not provide sufficient resources to enable them to achieve the rapid and sustained growth needed to reach various poverty alleviation targets set by the international community for the new millennium. Full implementation of commitments by most developing countries undertaken during the Uruguay Round, together with continued restrictions on market access in some major industrial countries, are generating payments deficits that cannot be financed on a sustained and reliable basis by international capital markets. Moreover, official financing is no longer available on a scale to fill this gap. The outcome of the Financing for Development conference does not by itself remove this inconsistency: the additional pledges made in the context of this conference fall short of the amounts needed to close the resource gap, which, according to a number of independent estimates, would require the doubling of official aid. This implies that many developing countries may have to accept slow growth that is unlikely to make much of a dent in poverty. On the other hand, as recent experience in several emerging markets shows, efforts to accelerate growth by greater reliance on private financial flows can make the matters worse by creating instability and boom-bust cycles, which, *inter alia*, harm the productive investment needed to improve trade performance.

- It is also widely believed that the existing arrangements do not allow sufficient policy space to developing countries to overcome their longer-term payments constraint by pursuing targeted trade, industrial and technology policies and thus increasing their export capacity in more dynamic sectors. There are increasing concerns that current policy orthodoxy and global arrangements have the result of kicking away the ladder by which today's advanced countries attained their present levels of economic development by denying developing countries many of the policy instruments that were widely and successfully used in the past.

- It is generally recognized that in a world of increased interdependence there should be a minimum degree of consistency and coherence between national and international policies. Indeed, multilateral rules and commitments circumscribe the policies that countries may apply within their national borders because of their global ramifications. Such multilateral discipline is particularly important for countries whose economic policies have a strong influence on the rest of the world. Although global checks and balances have been introduced in some sectors such as trade, they are not always effective vis-a-vis Governments in major industrial countries which often come under political pressures to protect domestic sectors. Moreover, for such countries similar checks and balances are absent or inadequate in a number of areas, including macroeconomic and financial policies, which are known to generate even stronger global repercussions than trade policies. By contrast macroeconomic and structural policies in most developing countries are subject to tighter surveillance in the multilateral financial institutions, even though the global impact of their national policies is much weaker.

19. The objectives pursued by the architects of the post-war international economic order, namely broad-based, rapid and sustained growth and development conducive to greater international economic integration, continue to be equally valid today. The best achievement of these goals now involves meeting even more complex policy challenges to ensure consistency and coherence among various components of the international economy, as well between these components and economic development. However, despite the increased recognition that the growth in global interdependence poses greater problems regarding the coherence, complementarity and coordination of global economic policy making, the mechanisms and institutions put in place over the past three decades have not been adequate for this challenge. Proposals in the current context of globalization should thus start with an attempt to address these problems, *inter alia* through the appropriate parts of the United Nations system. As recognized by the Bangkok Plan of Action (para. 103), UNCTAD has a unique role to play in this respect:

> Ensuring that all countries enjoy the benefits of globalization requires meeting complex policy challenges which arise, particularly at the global macroeconomic level, from the growing interdependence of the various spheres of economic activity, including particularly trade, finance and investment, and the downside risks which this interdependence sometimes carries. UNCTAD, as the focal point within the United Nations for the integrated treatment of trade and development and the interrelated issues in the

areas of finance, technology, investment and sustainable development, is eminently placed to examine these issues and to build consensus for reformulation of policies from a development perspective...

C. Rethinking development strategies

20. In almost all successful cases of rapid and sustained growth in developing countries a dramatic shift in economic structure from the primary sector to manufacturing has triggered a progressive rise in productivity and income levels. This rise has been sustained by a move from less to more technology- and capital-intensive activities both within and across sectors, and the resulting improvement in productivity performance has helped domestic producers compete on increasingly demanding international markets. The engine of this process of structural change and productivity growth has been a rapid and sustained pace of capital accumulation. Where the market and private property have assumed a prominent role, resources have been concentrated in the hands of a minority, whose behaviour has, to a large extent, determined the pattern of investment and growth. This process has rarely been a smooth one, and the need to manage the resulting tensions and conflicts have added a strong political dimension to "late industrialization".

21. In the past two decades, globalization has become the counterpoint to the policy issues surrounding late industrialization. Particularly since the debt crisis of the early 1980s, developing countries have been striving hard, and often at considerable cost, to integrate more closely into the global economy. The hope has been for an end to stop-go growth and development through export expansion and inflows of private foreign capital. Strategies for this purpose have required many developing countries to break with past policies and to pursue closer and faster integration into the world economy through rapid liberalization of trade, finance and investment. However, the past two decades have been characterized by slow and erratic growth, increased instability, and rising income gaps between most developing countries and the industrial world. This has led to the question of designing appropriate development strategies in a globalizing world.

22. While policies initially focussed on "getting the prices right", more recently the question of appropriate institutions, epitomized under the rubric of "good governance", has come to play a central role in the official policy advice to developing countries. The basic principles espoused for good governance generally include political accountability, participation and ownership, effective rule of law, and transparency and information flows. The pursuit of these principles is expected to result in good institutions such as democracy, an honest and efficient bureaucracy and judicial system, protection of property rights, good corporate governance and private and public finance systems, adequate social safety nets, protection of labour rights, etc. There is almost universal agreement on the importance of most of these principles and institutions in economic, social and political development at a general level. However, in assessing whether specific institutional arrangements are a prerequisite for rapid development in developing countries, it is important to keep in mind the following considerations:

- Historical experience shows that many of the institutions that are now regarded as prerequisites of successful economic development were actually the outcome rather than the cause of the economic development of today's advanced countries.
- Many developing countries today have much higher levels of institutional development compared to the level attained by today's industrialized countries when they were at similar levels of per capita income and economic development.
- Imposing a common institutional standard on all countries with different conditions is likely to be counterproductive: there is considerable institutional diversity even among industrial countries, and recent experience shows that many of the institutions of the advanced countries superimposed on existing economic, social and political structures in developing countries have failed to function properly.
- Efforts to adopt the institutions of developed countries may put considerable strain on financial and human resources in developing countries; they may also conflict with social and cultural norms.
- A number of institutions which were once held up as examples to be replicated (such as the bank-based financial system in East Asia or corporate governance in the United States) have subsequently been found to have serious weaknesses.

23. There can be little doubt that exaggerating these difficulties could easily become an excuse for defending the institutional status quo in developing countries. In fact, developing countries can still draw on the rich historical experience of today's advanced economies in creating or adopting institutions that can help foster development. Just as these countries have benefited immensely from technological advances in developed countries in areas such as medicine and industry to further human welfare without themselves having to innovate, they can equally learn and benefit from the institutional know-how and experience of developed countries. But levels of economic development and historical particularities set limits to what can be usefully replicated.

24. On the policy front, it is generally agreed that fiscal and monetary discipline and macroeconomic stability are a necessary but not a sufficient condition for sustained growth and development. Indeed, during the past decade most developing countries have made considerable progress in attaining fiscal discipline and price stability. The fact that greater price stability has not resulted in more vigorous and sustained growth has now led many to argue that attention should be turned to micro-level, supply-side policies. While such policies should always be integral components of targeted industrial and technology policies in developing countries, it is far from clear whether current difficulties have primarily microeconomic or macroeconomic origins. Even though inflation has been brought under control, macroeconomic stability has not been attained since key variables such as wages, exchange rates, and interest rates that exert a strong influence on investment and resource allocation have been extremely unstable in most developing countries, in large part because of increased financial instability associated with greater mobility of capital. A more stable and predictable macroeconomic environment is a prerequisite for a positive investment climate, and without it there is a risk that policies at the microeconomic level are much less likely to succeed.

25. So far the forces unleashed by rapid liberalization have favoured certain income groups over others without stimulating investment and growth. Furthermore, income inequality has increased almost everywhere as capital has gained in comparison with labour, and the wage gap between skilled and unskilled workers has widened in many countries. Financial liberalization has also given rise to a rapid expansion of public and private debt, to the benefit of a new rentier class, while agricultural liberalization in developing countries has favoured in many of them an urban trading class rather than farmers. These factors making for greater inequality have at the same time deterred investment and slowed growth because the groups that have benefited from liberalization have not invested their wealth in productive activities. In particular, the advantages given to global finance in terms of the speedy entry into and exit from financial markets in search of quick gains have often undermined the "animal spirits" needed to make longer-term commitments to investment in newly created productive assets.

26. In the light of these trends, the success of the late industrializing developing countries, mainly from East Asia, stands out. These experiences have provoked widespread interest and a good deal of controversy. However, there is a broad agreement that success in these countries has been based on the "high animal spirits" of their business class, reflected in exceptionally high rates of saving and investment from profits, and that a disciplined developmental state was instrumental in organizing these ingredients. From this perspective, the following elements of effective development strategies suggest themselves:

- For most poor countries, policies to accelerate investment and capital accumulation must initially be designed for a predominantly rural economy, with the basic aim of increasing agricultural productivity, particularly among smallholders, and generating a net agricultural surplus that can be used to nurture non-traditional activities. Predictable prices for inputs and final products, adequate rural credit, an appropriate exchange rate, public infrastructure investments, and specific supply-side policies to improve the technological capacities of farmers, to encourage market development and to minimise excessive risks are of crucial importance.

- As industrial activity begins to take off, a strategy to stimulate profitability and high levels of reinvestment of profits in productive activities will need to draw on fiscal measures as well as trade, financial and competition policies.

- The early stages of rapid growth, particularly as industry takes off, are likely to involve a significant financing gap as investment surges ahead of domestic savings. This gap needs to be filled initially by means of capital inflows, but should be gradually closed as domestic savings rise with rising income levels. This process of reducing dependence on international capital inflows is a distinct feature of successful industrialization and development. In many other countries periods of rapid growth failed to stimulate domestic savings with the result that when external trading and financial conditions deteriorated, growth could no longer be sustained. For a large majority of middle-income countries, an important challenge is how to reduce reliance on volatile international capital flows by

encouraging savings and capital accumulation, particularly through re-investment of a greater proportion of profits.

- Concerns about excessive reliance on external financing also raise issues as to whether market forces should determine the forms these flows take and their destination and use. Recent financial crises in developing countries leave little doubt that it is essential for them to manage capital flows so as to avoid boom-bust cycles and serious disruptions to growth and development.

27. Most developing countries also need to reorient the modalities of their participation in international trade. Indeed, while developing countries as a whole appear to have become more active and dynamic participants in world trade over the past two decades, on closer examination there has been a great deal of diversity in the channels of their participation in the international division of labour:

- First, many countries have not been able to move away from those primary commodities for which markets are relatively stagnant or declining. However, some countries have become successful exporters of more dynamic commodities and enjoyed rising incomes.
- Second, most developing countries that have been able to shift from primary commodities to manufactures have done so by focussing on resource-based, labour-intensive products, which generally lack dynamism in world markets
- Third, the apparent jump by some countries into skill- and technology-intensive products is often less than it seems, the reality being involvement in labour-intensive, assembly type activities in such products with relatively little value added
- Finally, a few countries, mainly from East Asia, have seen sharp increases in their shares in world manufacturing value added and world manufacturing trade, reflecting their steady progress in industrialization which predates the recent export drive elsewhere in the developing world

28. Most developing countries are still exporting resource- and labour-intensive products, effectively relying on their supplies of cheap labour to compete. But even as policy makers begin to see signs of success in terms of higher investment levels and rising market shares in labour- intensive manufactured exports, they need to anticipate future difficulties that these industries may face, including those due to rising wages, limits to productivity growth and deteriorating terms of trade. Overcoming these constraints requires gradual and purposeful nurture of a new generation of industries, particularly capital goods and intermediate products, with a greater potential for innovation, productivity growth and export dynamism. This requires measures to build and strengthen technological capacity at the national, industry and firm levels. Tax and other incentives can be used to encourage enterprise training along with a national programme at higher levels of education and greater industry-level involvement in vocational training schemes. Measures to facilitate local R&D, including financial subsidies, particularly for large and risky projects, the creation of science parks and special industrial estates offer potential ways of strengthening technological capacity.

29. Although a successful development strategy must be firmly based on the establishment of strong local firms linked to a dynamic accumulation process, there is little doubt that foreign firms are likely to have an important role at all stages in the development process. A variety of techniques can be used to maximize the advantages from interactions with foreign firms, from reverse engineering and licensing to the hosting of foreign affiliates. In most cases, a combination of such techniques is likely to be desirable, tailored to specific sectoral demands.

30. For poorer countries attempting to integrate at the low-cost end of the production chain, the very heavy import content of their activities poses one set of policy challenges. The potential technological and other spillovers, particularly for middle-income economies and in sectors where specific knowledge and capital equipment are closely knitted together, requires that host Governments preserve a range of policy options to enable them to bargain effectively with TNCs. Successful measures have in the past included regulation of FDI in areas where the aim is to nurture large domestic producers, domestic content agreements, and technology screening. In general, a more liberal approach to FDI is likely to bring significant benefits after productivity levels and technological capacities cross certain thresholds.

31. There are concerns among policy makers in developing countries that pursuing the kind of development strategies which have proved successful in the past is no longer feasible given the constraints of the emerging international economic order. Diminished sources of official financing and greater reliance on private capital flows are one source of potential constraint on policy options. Another source consists of the new obligations under the WTO, which subject domestic policies, particularly in the areas of industrial and technological development, to stricter disciplines than heretofore. Finally, conditionalities attached to multilateral loans have brought a wider set of policy measures under the close surveillance and assessment of the multilateral financial institutions. All these potential constraints need to be re-examined to ensure that developing countries have sufficient policy space to create the sort of investment-export nexus that can support rapid and sustained growth.

32. In effect, many developing countries are not using all the policy options open to them. Many of the financial, fiscal and sectoral policies that can help create the basic conditions for faster and better directed capital accumulation and channel investments in a manner consistent with broader development objectives are not governed by multilateral agreements. In particular the scope for export promotion, though reduced, still allows for various forms of support, particularly in the poorest countries.